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MIDWEST NATURAL GAS

CORPORATION

Washington, Indiana

INDIANA UTILITY REGULATORY COMMISSION

Case No. 43229

DIRECT TESTIMONY AND EXHIBITS OF

DAVID C. MERCER

IN WITNESS WHEREOF

EWG

MIDWEST NATURAL GAS CORPORATION
Washington, Indiana

FILED

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INDIANA UTILITY
REGULATORY COMMISSION

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DCM

MIDWEST NATURAL GAS CORPORATION
Washington, Indiana

INDIANA UTILITY REGULATORY COMMISSION
Cause No. 43229

DIRECT TESTIMONY OF

DUANE C. MERCER

MIDWEST NATURAL GAS CORPORATION
Washington, Indiana

IURC Cause No. 43229

Direct Testimony and Exhibits of

Duane C. Mercer

Q. 1. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Duane C. Mercer and my business address is One American Square,
Suite 2600 Indianapolis, Indiana 46282.

Q. 2. MR. MERCER, WHAT IS YOUR OCCUPATION?

A. I am a Certified Public Accountant with the London Witte Group, LLC, a firm,
which, specializes, in utility regulation before the Indiana Utility Regulatory
Commission.

**Q. 3. WOULD YOU PLEASE DESCRIBE YOUR EDUCATIONAL
BACKGROUND AND PROFESSIONAL QUALIFICATIONS, WHICH YOU
BELIEVE MIGHT BE RELEVANT TO THE PRE-FILED TESTIMONY AND
ORAL OPINIONS YOU OFFER?**

A. I am a 1969 graduate of Indiana University where I earned a Bachelor of Science
degree in Business, with a concentration in accounting and economics. Following
graduation, I was employed by the international accounting firm of Ernst & Young
where I performed financial and operational audits, director's examinations and
similar other services for a variety of clients. In 1972, RCA Consumer Electronics
Division employed me in the Internal Auditing Department where I managed in the
development and implementation of audit programs for all fiscal and administrative

1 areas of the Division. In 1976, I became Manager of International Finance for the
2 Consumer Electronics Division of RCA with primary responsibility for financial
3 planning, forecasting, and coordination of our foreign operating plants. In 1978, the
4 Consumer Counselor's office for the State of Indiana employed me as the staff
5 Certified Public Accountant. During my employment with the Consumer Counselor,
6 I advised that office on numerous utility issues coordinated the filings of the Fuel
7 Adjustment Clause and Gas Cost Adjustment with the consultants retained by that
8 office, and testified on their behalf as required. In July 1983, I established a practice
9 specializing in utility regulation. In 1985, I consolidated my practice with two other
10 practitioners and formed Brenner, Mercer & Perry, P.C. to also perform work in the
11 utility regulation area. Since May 1, 1987, I have been the Partner in charge of
12 Utility Services for London Witte Group, LLC, a Firm specializing in, among other
13 areas, utility regulation on behalf of the public, municipal and investor-owned
14 utilities, and intervenors before the Indiana Utility Regulatory Commission.

15
16 **Q. 4. WHAT ARE YOUR PROFESSIONAL AFFILIATIONS?**

17 A. I am a member of the American Institute of Certified Public Accountants, and the
18 Indiana Association of Certified Public Accountants, for which I have served as a
19 member of the Utilities Committee.

20
21 **Q. 5. ON WHOSE BEHALF ARE YOU APPEARING IN THIS CAUSE?**

22 A. I am appearing on behalf of Midwest Natural Gas CORPORATION
23

24 **Q. 6. WHAT IS THE SCOPE AND PURPOSE OF YOUR ASSIGNMENT?**

25 A. I and my Firm have been engaged by the Petitioner to analyze Petitioner's current

1 financial information and advise Petitioner and Petitioner's counsel as to changes in
2 various rates and charges that should be sought in order to better provide a reasonable
3 return on investment in used and useful property and cover all operation,
4 maintenance, and tax expenses of the utility. In providing such service, I have
5 reviewed Petitioner's books and records, examined Petitioner's capital structure, and
6 considered the costs associated with various elements of the capital structure, and
7 reviewed Commission's Orders in numerous cases, among other activities. On the
8 basis of my expertise, experience, and this analysis, I have been able to form various
9 opinions, as well as make recommendations to Petitioner's management regarding its
10 need for additional revenue. I have reduced these opinions, along with my
11 recommendations to the form of schedules, which are attached to Ms. Mann's and my
12 testimony.

13
14 **Q. 7. MR. MERCER, PLEASE SUMMARIZE THE MAJOR CONCLUSION THAT**
15 **YOU REACHED OR ANY CONCERNS THAT YOU HAVE FOLLOWING**
16 **YOUR ANALYSIS.**

17 **A.** Petitioner is not earning its authorized return on rate base approved in our last rate
18 case. Our last rate case was filed in 2002, based on a test year ending December 31,
19 2001, and was primarily a rate base update case. The major reason for filing this rate
20 case is not only to recover increased operating costs, but also to recover the loss of
21 revenue from several large industrial and commercial customers who have
22 discontinued operations since our last rate case. In addition to this lost usage we
23 have experienced a significant decline in the monthly usage by our remaining
24 commercial and firm industrial customers. In fact, this decline has continued through
25 2007. This decline in usage also contributes to the need for this rate adjustment.

1 These three factors, discussed above, account for the majority of the increase
2 requested in this cause. Permitting Petitioner to earn a return on its investment will
3 improve Petitioner's financial soundness, appropriately compensate it's investors for
4 their devotion of capital to the enterprise and assist in establishing rates sufficient to
5 cover all of its current operation expenses.

6
7 **Q. 8. WOULD YOU PLEASE DESCRIBE THE TECHNICAL EXHIBITS, WHICH**
8 **YOU SPONSOR?**

9 **A.** Yes, I am sponsoring Exhibit C, D, and Exhibit E as well as Schedules C-2, C-3
10 and portions of C-1. Exhibit C presents the "Pro-Forma Operating Income
11 Statement". It reflects the results of operations under differing assumptions. The
12 column entitled "August 31, 2006", reflects the actual per book results of
13 Petitioner's operations for the agreed upon test year. The column entitled "Pro-
14 Forma Present Rates" reflects the results of operations after the adjustments for all
15 fixed, known and measurable elements have been taken into account. The column
16 entitled "Proposed Rates" reflects the projected results of operations based upon a
17 recommended increase of approximately 8.91%. The "Adjustments" reflected on
18 Exhibit C are detailed on Schedules C-1, C-2 and C-3. Exhibit D reflects the
19 calculation of the Original Cost Rate Base at August 31, 2006. Exhibit E
20 summarizes the Cost of Capital calculation for Petitioner.

21
22 **Q. 9. PLEASE DESCRIBE THE ADJUSTMENTS PRESENTED IN SCHEDULE C-**
23 **1, WHICH ARE SPONSORED BY YOU?**

24 **A.** I am sponsoring **Adjustment No. 1 and Adjustment No. 2** as follows:
25 **Adjustment No. 1** which adjusts "Operating Revenue" is comprised of five (5)

1 separate adjustments totaling (\$21,205,852) as follows:

- 2 a) Elimination of (\$8,651,780) in Gas Cost Adjustment (GCA) Revenues
3 received during the test year ended August 31, 2006.
- 4 b) Increase in "Operating Revenue" of \$978,689 for weather normalization
5 resulting from approximately a 12% warmer than normal weather experience
6 during the test year on which these rates are to be set. Normal weather in this
7 calculation is the 30-year average of weather information on heating degree-
8 days from 1970 to 2000, as reported by NOAA weather. In accordance with
9 the weather normalization methodology approved in our most recent Normal
10 Temperature Adjustment (NTA) proceeding before this commission, we used
11 the approved blend of 75% Louisville and 25% Indianapolis as our test year
12 weather stations for this case.
- 13 c) Decrease in "Operating Revenue" of (\$2,166,584) for the loss of several large
14 commercial and firm industrial customers, as well as, decreased consumption
15 by our remaining customers during the test year, and continuing its decline
16 into 2007. This adjustment eliminates the revenue associated with these lost
17 customers and declining sales volume included in the test year.
- 18 d) Decrease in "Operating Revenue" of (\$28,603) resulting from the
19 reclassification of customers to the correct rate class for the test year.
- 20 e) Decrease of \$(11,337,574) in "Operating Revenues" to reflect the
21 synchronization of revenue to be collected through rates based on the changes
22 in the base cost of gas established in the last general rate proceeding and the
23 pro-forma cost of gas as detailed in Adjustment 2. As has been the practice
24 of most gas utilities, petitioner has removed the cost of natural gas as part of
25 its base rates in this case. As a result, gas costs will be recovered in the Gas

1 Cost Adjustment (GCA) process.

2 **Q. 10. WOULD YOU PLEASE DESCRIBE ADJUSTMENT NO. 2 FOR**
3 **PURCHASED GAS?**

4 **Adjustment 2** decreases the cost of "Natural Gas Purchased" by (\$21,303,901) to
5 eliminate the cost of gas from Petitioner's base rates. All gas costs incurred in the
6 future will be included in the GCA process as verified by the Office of Utility
7 Consumer Counselor, and approved by the IURC. The elimination of gas cost does
8 not in any way affect the amount of increase being sought in this proceeding.
9

10 **Q. 11. PLEASE DESCRIBE THE ADJUSTMENTS PRESENTED IN SCHEDULE C-**
11 **2, WHICH ARE SPONSORED BY YOU.**

12 **A.** **Adjustment A**, of Schedule C-2, reflects the projected proposed increase in annual
13 revenue of \$2,048,995 assuming the proposed rates are granted. **Adjustments B, C,**
14 **D, and E** of \$2,176, \$9,989, \$28,546 and \$797,083, respectively reflect the proposed
15 increases in the IURC fee, the bad debt expense, the 1.4% State Utility Receipts Tax,
16 the State and the Federal Income Tax associated with the proposed 8.91% increase in
17 rates requested in this filing. In my opinion, I believe each of the adjustments I have
18 made is proper and has been made in accordance with the classification of accounts
19 approved by the Commission for utilities of the class of Petitioner.
20

21 **Q. 12. BASED UPON THE AFOREMENTIONED FIXED, KNOWN AND**
22 **MEASURABLE ADJUSTMENTS, WHAT IS THE PROJECTED PRO-**
23 **FORMA PRESENT RATE NET OPERATING INCOME?**

24 **A.** The Pro-Forma Present Rates Net Operating Income is projected to be \$1,104,364
25 which is less than what was authorized as a reasonable net operating income in 2003.

1 This is an increase of \$1,211,201 from the present Pro Forma rate Net Operating
2 Loss of (\$106,837) as reflected on Exhibit C. Exhibit C-3 provides the calculation of
3 the overall revenue adjustment as well as the average percent increase a typical
4 customer will experience.

5 **Q. 13. MR. MERCER, WOULD YOU PLEASE DESCRIBE EXHIBIT D?**

6 A. Yes. Exhibit D is the calculation of Original Cost Rate Base. It is comprised of
7 several components.

8
9 **Q. 14. WHAT ARE THOSE COMPONENTS?**

10 A. The major component is Utility Plant-in-Service as of August 31, 2006. This total is
11 \$26,415,761. The subtraction of accumulated depreciation of \$15,489,505 results in
12 the Net Utility Plant in Service of \$10,926,256.

13 To the Net Utility Plant-in-Service, we have added our requirement for cash working
14 capital in the amount of \$481,733 using the FERC 45-day working capital formula.
15 This methodology has been accepted for gas utilities the size of Petitioner in lieu of
16 performing a cash lead-lag study.

17 Additionally, we have included the 13-month average of material and supplies in the
18 amount of \$454,138.

19 The total original cost rate base being requested in this Cause is \$11,862,127.
20

21 **Q. 15. PLEASE CONTINUE WITH THE EXPLANATION OF YOUR EXHIBITS.**

22 A. Exhibit E presents the "Cost of Capital Calculation" using the capital structure as of
23 August 31, 2006, and using the 11.75% return on Common Equity. Schedule E is the
24 Calculation of the Overall Weighted Cost of Capital of 9.31%. Schedule E-1 is the
25 Calculation of Synchronized Interest, which is used as a component for the

1 calculation of State and Federal Income Tax expense.

2
3 **Q. 16. MR. MERCER, HAVE YOU PREVIOUSLY TESTIFIED BEFORE THIS**
4 **COMMISSION ON AN APPROPRIATE AND REASONABLE RATE OF**
5 **RETURN ON EQUITY FOR INVESTOR-OWNED UTILITIES?**

6 **A.** Yes. I have testified before this Commission on numerous occasions on such a
7 subject, including previously on behalf of Petitioner.

8
9 **Q. 17. HAVE YOU FORMED AN OPINION AS TO WHAT A REASONABLE RATE**
10 **OF RETURN ON EQUITY WOULD BE FOR THIS PETITIONER WHICH**
11 **WOULD ALSO BE REASONABLE FOR THE FORESEEABLE FUTURE?**

12 **A.** Yes, I have.

13
14 **Q. 18. PLEASE EXPLAIN WHAT YOUR OPINION IS AND GENERALLY HOW**
15 **YOU ARRIVED AT SUCH OPINION.**

16 **A.** I believe the rate of return on equity should be at least 11.75%. I have arrived at such
17 opinion from a variety of considerations. First, I considered the Commission's oft
18 quoted requirements of the purpose of a reasonable return. Namely, that such a
19 return is one which is comparable to returns of others having corresponding risks, is a
20 return which is sufficient to ensure confidence and financial integrity of the regulated
21 utility, is sufficient to maintain its current credit, and will allow the utility to attract
22 capital.

23 Next I considered the risk associated with the procurement of natural gas,
24 competition with alternative fuels, and credit concerns by suppliers to small gas
25 utilities and the GCA process itself. Accordingly, some component of these factors

1 should be considered in the rate of return requested by a utility.

2 In addition, I also reviewed what Petitioner has been able to earn based on the last 21
3 quarters of the GCA process. Based on that review I noted that Petitioner has a
4 negative Operational Income Earnings Test pool differential of (\$13,128,798)
5 or (\$1,025,011) on an annual accumulation basis. This deficit pool of earning is
6 almost equal to the net operating income being requested by Petitioner today. Again,
7 this factor should also be considered in developing a return for this utility.

8 Arguably, given the risk of uncertainty resulting from natural gas procurement,
9 competition from competing fuels, as well as the fact that Petitioner has under earned
10 its previously authorized return in 21 consecutive GCA quarters, Petitioner should be
11 authorized a return commensurate with it perceived overall risk.

12 Finally, I took into consideration the fact that not only is Petitioner's stock unlisted
13 on any exchange, but it is also a small utility without some of the tools that other
14 larger utilities have for ensuring a greater recovery of their authorized net operating
15 income. Therefore additional consideration should be given to both the company's
16 size, as well as its lack of liquidity of the stock as the Commission has considered in
17 prior cases.

18 Taking all of these considerations together and recognizing that Petitioner is trying to
19 retain the confidence of its stockholders, I am of the opinion that an 11.75% return on
20 equity is a minimum return that this Commission should authorize in this proceeding.

21
22 **Q. 19. MR. MERCER, HAVE YOU INCLUDED IN YOUR ADJUSTMENTS FOR**
23 **RATE CASE EXPENSE COSTS OF HIRING AN ECONOMIST TO SPEAK**
24 **TO THE ISSUE OF RATE OF RETURN ON EQUITY?**

25 **A.** Yes, I have.

1 **Q. 20. I NOTE THAT NO ECONOMIST HAS FILED DIRECT TESTIMONY IN**
2 **THIS CASE. WHY WOULD SUCH RATE CASE EXPENSE BE**
3 **NECESSARY?**

4 **A.** I have included this expense based upon the anticipated analysis by and preparation
5 of exhibits from an additional expert with experience in evaluating appropriate utility
6 returns. I anticipate rebuttal will be necessary to the testimony filed by the Office of
7 Utility Consumer Counselor based upon historical testimony filed relative to this
8 Petitioner and other similarly situated petitioners. To the extent that rebuttal
9 testimony of the economist is not filed, this amount can be reduced in my rate case
10 expense adjustment.
11

12 **Q. 21. MR. MERCER, IN YOUR OPINION, WHAT IS THE AMOUNT OF**
13 **INCREASE IN REVENUES THAT IS REQUIRED BY THE PETITIONER IN**
14 **ORDER TO RECOVER THE CURRENT COST OF SERVICE INCLUDING**
15 **A REASONABLE RETURN ON ITS USED AND USEFUL PROPERTY?**

16 **A.** Based on my analysis and the findings on my exhibits, the Petitioner should be
17 authorized to increase rates and charges by an amount sufficient to generate
18 \$2,048,995 in additional Operating Revenue. This recommended increase would
19 result in total Pro-Forma Proposed Revenues of \$7,020,859. Other operating
20 revenues are \$185,718. Deducting Pro-Forma Proposed Operating Expenses of
21 \$6,102,213 produces a Pro-Forma Proposed Net Operating Income of \$1,104,364.
22

23 **Q. 22. IF THIS COMMISSION AUTHORIZED A NET OPERATING INCOME OF**
24 **\$1,104,364, WHAT IS THE OVERALL RATE OF RETURN ON**
25 **PETITIONER'S USED AND USEFUL PLANT?**

1 A. A Net Operating Income of \$1,104,364 would result in a 9.31% overall return on the
2 original cost rate base. The components comprising the overall return are detailed on
3 Exhibit E.
4

5 **Q. 23. HAVE YOU ALSO EXAMINED PETITIONER'S RATE BASE AND BEEN**
6 **ABLE TO MAKE A DETERMINATION AS TO THE ORIGINAL COST?**

7 A. Yes, I have. Based upon Petitioner's books and records and my discussions with
8 management, I believe the original cost is no less than \$11,862,127.
9

10 **Q. 24. MR. MERCER, ON THE BASIS OF YOUR ANALYSIS, WHAT NET**
11 **OPERATING INCOME SHOULD THIS PETITIONER BE AUTHORIZED**
12 **AN OPPORTUNITY TO EARN?**

13 A. I believe this Petitioner should be authorized a reasonable opportunity to earn
14 \$1,104,364.
15

16 **Q. 25. WILL PETITIONER'S CUSTOMERS SEE AN INCREASE OR A**
17 **DECREASE DUE TO THIS CHANGED NET OPERATING INCOME?**

18 A. The Petitioner's customers will see an increase due to this changed Net Operating
19 Income. The exact amount of the increase will be based on the cost of service study
20 performed by Mr. Kerry Heid of Heid Rate Consulting.
21

22 **Q. 29. DOES THAT CONCLUDE YOUR TESTIMONY?**

23 A. Yes sir, it does.

BJM

MIDWEST NATURAL GAS CORPORATION, INC.
Washington, Indiana

INDIANA UTILITY REGULATORY COMMISSION
Cause No. 43229

PRE-FILED DIRECT TESTIMONY OF

BONNIE J. MANN

MIDWEST NATURAL GAS CORPORATION, INC.
Washington, Indiana

IURC Cause No. 43229

**Pre-filed Direct Testimony of
Bonnie J. Mann**

Q. 1. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Bonnie J. Mann; my business address is One American Square, Suite 2600, Indianapolis, Indiana 46282.

Q. 2. WHAT IS YOUR OCCUPATION?

A. I am a Certified Public Accountant specializing in public utility matters.

Q. 3. BY WHOM ARE YOU EMPLOYED?

A. I am employed by London Witte Group, LLC. (LWG)

Q. 4. WOULD YOU PLEASE DESCRIBE YOUR EDUCATIONAL BACKGROUND AND PROFESSIONAL QUALIFICATIONS?

A. I am a 1987 graduate of Butler University where I earned a Bachelor of Science Degree in business, with a concentration in accounting. Following graduation, I was employed by the international accounting firm of Peat Marwick, where I performed financial and operational audits for a variety of clients. Since September 1988, I have been employed by London Witte Group, LLC, and I am currently a Principal concentrating in the utilities area.

Q. 5. WHAT ARE YOUR PROFESSIONAL AFFILIATIONS?

1 A. I am a member of the Indiana Association of Certified Public Accountants (ICPA),
2 and the American Institute of Certified Public Accountants (AICPA). I have been a
3 member of the ICPA Utilities Committee.
4

5 **Q. 6. WHAT IS THE SCOPE AND PURPOSE OF YOUR ASSIGNMENT?**

6 A. The scope and purpose of my assignment was to assist Mr. Mercer in the review of
7 Petitioner's financial records in order to form an opinion as to the appropriate level of
8 revenues required to recover the Petitioner's current cost of service and to prepare
9 Testimony and Exhibits in the Petitioner's behalf for presentation to the IURC in the
10 form of evidence supporting Petitioner's request.
11

12 **Q. 7. ON WHOSE BEHALF ARE YOU APPEARING IN THIS CAUSE?**

13 A. I am appearing on behalf of Midwest Natural Gas Corporation, Inc.
14

15 **Q. 8. I HAND YOU A DOCUMENT MARKED AS PETITIONER'S EXHIBITS**
16 **BJM AND DCM-1 AND ASK YOU TO IDENTIFY THEM.**

17 A. Exhibit BJM is my Pre-filed written testimony, and Exhibit DCM-1 is comprised of
18 the technical exhibits and supporting schedules which are used as a basis for our
19 opinion as to the appropriate level of revenues. I have worked in conjunction with
20 Mr. Mercer in developing these supporting schedules.
21

22 **Q. 9. WOULD YOU PLEASE EXPLAIN THE TECHNICAL EXHIBITS WHICH,**
23 **YOU SPONSOR?**

1 A. Yes. Exhibit A and B show the audited Comparative Balance Sheets and Statements
2 of Net Income, respectively, for the Petitioner. This historical information is
3 presented as of August 31, 2006, and August 31, 2005, and for the years ended on
4 each of said dates. The twelve months ended August 31, 2006, is the test year
5 approved in the Pre-Hearing Order in this Cause. The books and records of petitioner
6 are kept in accordance with the uniform system of accounts for a gas utility. They are
7 the representations of the management of the Petitioner, and are the starting point for
8 our adjustments. Schedules A-1, B-1 and B-2 are the supporting detail for the major
9 Balance Sheet and Statement of Income elements, respectively. All of the amounts
10 presented in Exhibits A and B as well as Schedules A-1, B-1 and B-2 come directly
11 from the Petitioner's audited financial statements for the years ended August 31,
12 2006 and 2005. In addition, I am sponsoring certain adjustments in schedule C-1.

13
14 Q. 10. **WOULD YOU PLEASE DESCRIBE THE ADJUSTMENTS CONTAINED IN**
15 **SCHEDULE C-1, WHICH ARE SPONSORED BY YOU?**

16 A. Yes, **Adjustment No.'s 3, 4, 5, 6, and 7** are comprised of several adjustments to
17 "Operating Expenses".

18
19 **Adjustment No. 3** adjusts "Operation and Maintenance" expense and consists of
20 three (3) different adjustments totaling \$221,755 as follows:

- 21 a) Increase in net payroll expense effective within twelve (12) months from the
22 end of the test period, of \$184,168. Pro-forma payroll was calculated by
23 annualizing the test year payroll by employee and then making additional

1 adjustments for salary increases expected in July 2007, the Petitioners normal
2 date for payroll increases.

- 3 b) Increase in "Operation and Maintenance" expense of \$39,858, representing the
4 amortization of the current rate case expenses of \$200,00 in professional fees
5 and \$7,000 in mailing expenses over the expected life of the proposed rates,
6 which we estimate to be three (3) years.
- 7 c) Decrease in IURC fee of (\$2,271) to reflect the current IURC rate on the
8 applicable Pro-Forma Present Rate Revenues.

9
10 **Adjustment 4** consists of six adjustments to "Administrative and General" expense
11 totaling \$69,718 as follows:

- 12 a) Increase in "Administrative and General" expense to reflect the change in the cost
13 of property and casualty insurance of \$11,098.
- 14 b) Increase in "Administrative and General" expenses to reflect the increase in the
15 cost of health and life insurance of \$16,381.
- 16 c) Increase in Administrative and General" expense for the increase in the ESOP
17 cost of \$11,050. This increase is based on the Proforma salaries calculated for the
18 payroll adjustment described above.
- 19 d) Decrease in "Administrative and General" expenses to reflect the removal of rent
20 included in the test year of (\$57,600), as a result of the purchase of the office
21 buildings for the Scottsburg and Bloomfield operational service center.
- 22 e) Increase "Administrative and General" expense by \$64,227 for miscellaneous
23 expense changes including communications expense, public awareness programs,

1 additional outside professional fees and office expenses.

- 2 f) Increase to "Administrative and General" expense by \$24,562 to reflect the
3 requested amortization of the cost of the NTA proceeding over a 3 year period.
4

5 **Adjustment 5** reflects the increase in the pro-forma "Depreciation and Amortization
6 Expense" for the Utility Plant-In-Service as of August 31, 2006, which is the
7 approved cut-off date for Utility Plant-In-Service. We have calculated depreciation
8 using 3.75% rate for distribution plant, a 20% rate for transportation and computer
9 equipment, a 10% rate for office, tools and communication equipment. This results
10 in an increase in Depreciation of \$79,359. The Commission previously approved
11 these depreciation rates.
12

13 **Adjustment 6** is comprised of two (2) adjustments totaling (\$283,146) to "Taxes
14 Other Than Income Taxes" as follows:

- 15 a) To adjust payroll taxes by \$12,861 for the increase in payroll reflected in
16 Adjustment 3 a.
17 b) Decrease in Utility Receipts Tax of (\$296,007) to reflect the Pro-Forma
18 Present Rate adjustments to revenues multiplied by the Utility Receipts Tax
19 Rate of 1.4%.
20

21 **Adjustment 7** is comprised of two (2) adjustments increasing Income Taxes by
22 \$26,930 after considering the afore-mentioned adjustments to revenues and expenses
23 as follows:

1 a) Decrease in State Income Tax of (\$11,412).

2 b) Increase in Federal Income Tax of \$38,342.

3

4 **Q. 11. DOES THAT CONCLUDE YOUR TESTIMONY?**

5 **A.** Yes sir, it does.

DCM-1

MIDWEST NATURAL GAS CORPORATION
Washington, Indiana

INDIANA UTILITY REGULATORY COMMISSION
Cause No. 43229

EXHIBITS OF

DUANE C. MERCER

AND

BONNIE J. MANN

MIDWEST NATURAL GAS CORPORATION

**Comparative Balance Sheets
August 31, 2006 and 2005**

| | As of | |
|---|----------------------------|----------------------------|
| | <u>2006</u> | <u>2005</u> |
| <u>ASSETS</u> | | |
| <u>UTILITY PLANT</u> | | |
| Utility Plant-in-Service | \$ 26,518,385 | \$ 25,407,382 |
| Less: Accumulated Depreciation | <u>(15,489,505)</u> | <u>(14,694,003)</u> |
| Net Utility Plant | <u>11,028,880</u> | <u>10,713,379</u> |
| <u>NON-CURRENT ASSETS</u> | | |
| Investments | 410,506 | 447,688 |
| Other Non-Current Assets | <u>555,920</u> | <u>604,130</u> |
| Total Non-Current Assets | <u>966,426</u> | <u>1,051,818</u> |
| <u>CURRENT ASSETS</u> | | |
| Cash | 138,138 | 773,367 |
| Accounts Receivable | 3,191,316 | 2,751,937 |
| Inventory | 424,861 | 429,123 |
| Prepaid Expenses and Other Current Assets | <u>565,195</u> | <u>448,283</u> |
| Total Current Assets | <u>4,319,510</u> | <u>4,402,710</u> |
| TOTAL ASSETS | <u><u>\$16,314,816</u></u> | <u><u>\$16,167,907</u></u> |

MIDWEST NATURAL GAS CORPORATION

**Comparative Balance Sheets
August 31, 2006 and 2005**

| | As of | |
|--|----------------------------|----------------------------|
| | 2006 | 2005 |
| <u>LIABILITIES AND STOCKHOLDER'S EQUITY</u> | | |
| <u>STOCKHOLDER'S EQUITY</u> | | |
| Common Stock Issued | \$ 723,341 | \$ 723,341 |
| Other Paid-in Capital | 222,352 | 222,352 |
| Treasury Stock | (10,087,937) | (9,149,756) |
| Retained Earnings | <u>17,861,483</u> | <u>18,390,518</u> |
| Total Shareholders' Equity | <u>8,719,239</u> | <u>10,186,455</u> |
| <u>LONG TERM LIABILITIES</u> | | |
| Long Term Debt | <u>3,874,242</u> | <u>3,294,918</u> |
| Total Long Term Liabilities | <u>3,874,242</u> | <u>3,294,918</u> |
| <u>CURRENT LIABILITIES</u> | | |
| Current Portion of Long Term Debt | 305,423 | 192,767 |
| Notes Payable (Receivable) - Intercompany | 209,484 | (773,595) |
| Accounts Payable | 1,598,046 | 1,595,968 |
| Customer Deposits and Advances | 345,280 | 347,427 |
| Accrued Liabilities | <u>254,318</u> | <u>259,760</u> |
| Total Current Liabilities | <u>2,712,551</u> | <u>1,622,327</u> |
| <u>ACCUMULATED DEFERRED INCOME TAXES</u> | <u>1,008,784</u> | <u>1,064,207</u> |
| TOTAL LIABILITIES AND EQUITY | <u>\$16,314,816</u> | <u>\$16,167,907</u> |

MIDWEST NATURAL GAS CORPORATION**Detail of Utility Plant-in-Service
August 31, 2006 and 2005**

| <u>Description</u> | <u>2006</u> | As of | <u>2005</u> |
|--|---------------------|--------------|---------------------|
| <u>Utility Plant in Service</u> | | | |
| <u>Transmission Plant</u> | | | |
| Land and Land Rights Transmission | \$ 146,435 | \$ | 146,435 |
| Right of Way | 109,233 | | 109,233 |
| Land Transmission from PG | 1,500 | | 1,500 |
| Easements Transmission from PG | 59,757 | | 59,757 |
| Structures and Improvements | 3,997 | | 3,997 |
| Intermediate Mains | 7,002,294 | | 6,904,877 |
| Meas and Reg Station Equip | 282,297 | | 278,215 |
| Communication Equipment | 65,193 | | 51,752 |
| | <u>7,670,706</u> | | <u>7,555,766</u> |
| Transmission Plant | | | |
| <u>Distribution Plant</u> | | | |
| Land and Land Rights Distribution | 119,053 | | 119,053 |
| Structures and Improvements | 10,779 | | 6,129 |
| Distribution Mains | 7,016,219 | | 6,915,976 |
| Meas and Reg Station General | 239,131 | | 238,251 |
| Meas and Reg City Gate | 300,643 | | 255,118 |
| Services | 5,223,558 | | 5,173,453 |
| Meters | 1,569,053 | | 1,575,753 |
| Meter Installation | 172,939 | | 166,352 |
| House Regulators | 747,485 | | 731,900 |
| House Reg Installations | 97,195 | | 95,210 |
| Industrial Meas and Reg | 496,893 | | 489,212 |
| Other Equipment | 33,491 | | 22,790 |
| | <u>\$16,026,439</u> | | <u>\$15,789,197</u> |
| Distribution Plant | | | |

MIDWEST NATURAL GAS CORPORATION**Detail of Utility Plant-in-Service****August 31, 2006 and 2005**

| <u>Description</u> | 2006 | As of 2005 |
|--|----------------------------|----------------------------|
| <u>General Plant</u> | | |
| Land and Land Rights General | \$ 20,000 | \$ 20,000 |
| Structures and Imp General | 940,587 | 319,627 |
| Office Furniture and Equipment | 100,203 | 99,397 |
| Computer Equipment | 82,075 | 82,108 |
| Transportation Equipment | 683,348 | 653,725 |
| Tool and Garage Equipment | 34,835 | 31,954 |
| Laboratory Equipment | 12,096 | 12,096 |
| Power Operated Equipment | 182,558 | 182,847 |
| Communication Equipment | 56,297 | 45,187 |
| Other General Equipment - PG | 106 | 700 |
| General Plant | <u>2,112,105</u> | <u>1,447,641</u> |
| <u>Construction In Progress</u> | | |
| Salem City Gate | 0 | 8,267 |
| Clearing Champions Pointe | <u>102,624</u> | <u>0</u> |
| Total Construction in Progress | <u>102,624</u> | <u>8,267</u> |
| <u>Production Plant</u> | | |
| Organization | 8,512 | 8,512 |
| Franchise and Consent | 29,503 | 29,503 |
| Misc Intangible Plant | 850 | 850 |
| Land and Land Rights | 11,645 | 11,645 |
| Sears Production Plant | 21,374 | 21,374 |
| Plainville Production Plant | 8,175 | 8,175 |
| Plainville Gathering Lines | 13,942 | 13,942 |
| Sears Measure and Reg Equip | 4,372 | 4,372 |
| Plainville Measure and Reg Equip | 3,606 | 3,606 |
| Production Purification | 24,782 | 24,782 |
| Plainville Purification Equip | 1,634 | 1,634 |
| Structures and Improv Shaw | 19,372 | 19,372 |
| Shaw Wells | 233,956 | 233,956 |
| Shaw Plant Lines | 38,721 | 38,721 |
| Compressor Station Equip | 79,610 | 79,610 |
| Measuring and Reg Equip | 45,286 | 45,286 |
| Purification | <u>61,171</u> | <u>61,171</u> |
| Total Production Plant | <u>606,511</u> | <u>606,511</u> |
| Total Utility Plant in Service | <u><u>\$26,518,385</u></u> | <u><u>\$25,407,382</u></u> |

MIDWEST NATURAL GAS CORPORATION**Comparative Statements of Net Income
Years Ended August 31 2006 and 2005**

| <u>Description</u> | Years Ended | |
|--|---------------------------|-------------------------|
| | <u>2006</u> | <u>2005</u> |
| <u>Operating Revenues</u> | | |
| Gas Sales | \$26,177,716 | \$20,800,206 |
| Other Operating Revenues | 185,718 | 179,043 |
| Total Operating Revenues | <u>26,363,434</u> | <u>20,979,249</u> |
| <u>Operating Expenses</u> | | |
| Operation and Maintenance: | | |
| Natural Gas Purchased | 21,398,968 | 15,088,409 |
| Operation | 947,487 | 867,835 |
| Maintenance | 380,857 | 207,461 |
| Customer Accounts | 688,058 | 679,480 |
| Administrative and General | 1,545,985 | 1,483,676 |
| Total Operation and Maintenance | 24,961,355 | 18,326,861 |
| Depreciation | 1,044,063 | 1,044,016 |
| Taxes Other Than Income Taxes | 691,266 | 631,872 |
| Federal Income Taxes | (242,980) | 106,213 |
| Total Operating Expenses | <u>26,453,704</u> | <u>20,108,962</u> |
| Net Operating Income | <u>(90,270)</u> | <u>870,287</u> |
| <u>Other Income/Expense</u> | | |
| Interest expense | (254,133) | (241,187) |
| Interest and dividend income | 101,690 | 105,721 |
| Gain (loss) on disposition of property | 1,476 | 12,101 |
| Other income (expense), net | (2,585) | 7,142 |
| Total Other Income/Expense - Net | <u>(153,552)</u> | <u>(116,223)</u> |
| Net Income | <u><u>(\$243,822)</u></u> | <u><u>\$754,064</u></u> |

MIDWEST NATURAL GAS CORPORATION**Comparative Detail of Operating Revenues
Years Ended August 31 2006 and 2005**

| <u>Description</u> | Years Ended | |
|---------------------------------------|----------------------------|----------------------------|
| | <u>2006</u> | <u>2005</u> |
| <u>Gas Sales</u> | | |
| Residential | \$11,704,040 | \$9,754,954 |
| Commercial | 6,305,643 | 4,802,506 |
| Industrial | 5,707,130 | 4,106,912 |
| Public Authorities | 1,939,349 | 1,474,951 |
| Transport | 521,554 | 660,883 |
| Total Gas Sales | <u>26,177,716</u> | <u>20,800,206</u> |
| <u>Other Operating Revenue</u> | | |
| Forfeited Discounts | 108,848 | 95,818 |
| Miscellaneous Service Revenue | <u>76,870</u> | <u>83,225</u> |
| Total Other Operating Revenue | <u>185,718</u> | <u>179,043</u> |
| Total Operating Revenue | <u><u>\$26,363,434</u></u> | <u><u>\$20,979,249</u></u> |

MIDWEST NATURAL GAS CORPORATION**Comparative Detail of Operating Expenses
Years Ended August 31 2006 and 2005**

| <u>Description</u> | <u>Years Ended</u> | |
|--|--------------------|-------------------|
| | <u>2006</u> | <u>2005</u> |
| <u>Natural Gas Purchased</u> | | |
| Natural Gas Purchased | \$21,714,841 | \$15,474,679 |
| Less: Gas Cost Adjustments | (315,873) | (386,270) |
| Total Natural Gas Purchased | <u>21,398,968</u> | <u>15,088,409</u> |
| <u>Operation</u> | | |
| Operation Underground Shaw | 436 | 7,020 |
| Intermediate Supervision | 6,078 | 5,524 |
| Operation Meas and Reg Station | 44,292 | 49,072 |
| Dist Operation Supervision | 38,720 | 42,858 |
| Operations Mains and Service | 534,704 | 458,391 |
| Meas and Reg Station City Gate | 13,943 | 18,320 |
| Meter and House Regulator | 245,697 | 223,189 |
| Customer Installation | 4,067 | 4,448 |
| Gas Storage | 25,717 | 27,679 |
| Rents | <u>33,833</u> | <u>31,334</u> |
| Total Operation | <u>947,487</u> | <u>867,835</u> |
| <u>Maintenance</u> | | |
| Mains | 77,048 | 27,661 |
| Meter/Regulator City Gate | 2,238 | 1,638 |
| Measuring & Regulating | 26,652 | 9,047 |
| Services | 83,363 | 41,740 |
| Maint Other Equipment | 29,822 | 26,697 |
| Meters & Regulators | <u>161,734</u> | <u>100,678</u> |
| Total Maintenance | <u>380,857</u> | <u>207,461</u> |
| <u>Customer Accounts Expenses</u> | | |
| Communication Expense | 58,094 | 56,550 |
| Customer Supervision | 25,116 | 32,999 |
| Customer Meter Reading | 94,482 | 94,373 |
| Customer Operation | 381,839 | 338,348 |
| Uncollectible Accounts | <u>128,527</u> | <u>157,210</u> |
| Total Customer Accounts Expenses | <u>\$688,058</u> | <u>\$679,480</u> |

MIDWEST NATURAL GAS CORPORATION**Comparative Detail of Operating Expenses
Years Ended August 31 2006 and 2005**

| <u>Description</u> | <u>Years Ended</u> | |
|---|---------------------|---------------------|
| | <u>2006</u> | <u>2005</u> |
| <u>Administrative & General</u> | | |
| Administration & General Salaries | \$304,488 | \$279,462 |
| Office Supplies & Expenses | 263,674 | 289,621 |
| Advertising | 3,566 | 5,930 |
| Outside Services | 150,343 | 138,398 |
| Property Insurance | 84,567 | 84,461 |
| Injuries and Damages | 19,961 | 20,090 |
| Employee Benefits | 492,246 | 455,203 |
| Regulatory Commission Expense | 120,630 | 103,956 |
| Office Grounds Expense | 13,936 | 15,756 |
| Rents | 57,600 | 57,600 |
| Miscellaneous General Expenses | 34,974 | 33,199 |
| Total Administration & General Expenses | <u>1,545,985</u> | <u>1,483,676</u> |
| Total Operation & Maintenance | <u>3,562,387</u> | <u>3,238,452</u> |
| <u>Depreciation</u> | <u>1,044,063</u> | <u>1,044,016</u> |
| <u>Taxes Other Than Income Taxes</u> | | |
| Property Taxes | 206,838 | 229,125 |
| Utility Receipts Tax | 366,199 | 289,221 |
| Payroll Taxes -FICA | 118,229 | 113,526 |
| Total Taxes Other Than Income Taxes | <u>691,266</u> | <u>631,872</u> |
| <u>Income Taxes</u> | | |
| Federal Income Taxes | (253,088) | 116,498 |
| State Income Taxes | (29,829) | 70,833 |
| Deferred Income Tax | 39,937 | (81,118) |
| Total Income Taxes | <u>(242,980)</u> | <u>106,213</u> |
| Total Operating Expenses | <u>\$26,453,704</u> | <u>\$20,108,962</u> |

MIDWEST NATURAL GAS CORPORATION

**Pro-Forma Operating Income Statement
At Pro-Forma Present and Proposed Rates
For the 12 Months Ended August 31, 2006**

| | | | | Increase required | | | <u>8.91%</u> |
|-----------------------------------|----------------------------|---------------------|------------|--|--------------------|------------|---------------------------|
| <u>Description</u> | <u>August 31, 2006</u> | <u>Adjustments</u> | <u>Ref</u> | <u>Pro-Forma Present Rates</u> | <u>Adjustments</u> | <u>Ref</u> | <u>Proposed Rates</u> |
| <u>Operating Revenues:</u> | | | | | | | |
| Sales of Gas | \$26,177,716 | (\$21,205,852) | (1) | \$4,971,864 | \$2,048,995 | (A) | \$7,020,859 |
| Other Operating Revenues | 185,718 | | | 185,718 | | | 185,718 |
| Total Operating Revenues | <u>26,363,434</u> | <u>(21,205,852)</u> | | <u>5,157,582</u> | <u>2,048,995</u> | | <u>7,206,577</u> |
| <u>Operating Expenses:</u> | | | | | | | |
| Natural Gas Purchased | 21,398,968 | (21,303,901) | (2) | 95,067 | | | 95,067 |
| Other Operation & Maintenance | 3,562,387 | 291,473 | (3 & 4) | 3,853,860 | 12,165 | (B) | 3,866,025 |
| Depreciation and Amortization | 1,044,063 | 79,359 | (5) | 1,123,422 | | | 1,123,422 |
| Taxes Other Than Income Taxes | 691,266 | (283,146) | (6) | 408,120 | 28,546 | (C) | 436,666 |
| Income Taxes | (242,980) | 26,930 | (7) | (216,050) | 797,083 | (D) | 581,033 |
| Total Operating Expenses | <u>26,453,704</u> | <u>(21,189,285)</u> | | <u>5,264,419</u> | <u>837,794</u> | | <u>6,102,213</u> |
| Net Operating Income | <u>(\$90,270)</u> | <u>(\$16,567)</u> | | <u>(\$106,837)</u> | <u>\$1,211,201</u> | | <u>\$1,104,364</u> |

MIDWEST NATURAL GAS CORPORATION

**Detail of Adjustments
(WITNESS -MERCER)**

(1) REVENUE ADJUSTMENTS

(a)

Decrease in "Operating Revenue" from the elimination of GCA Revenues included in the test year.

(\$8,651,780)

(b)

To adjust "Operating Revenue" for the normalization of weather.

MIDWEST GAS DIVISION

| | Rate A | Rate B |
|--|------------------|------------------|
| Sales | 7,101,595 | 4,308,261 |
| Reclassified Load | | (16,124) |
| Less Lost Load | 0 | (491,201) |
| Base Load | 1,346,148 | 1,288,292 |
| Reclassified Load | | (22,880) |
| Less Lost Load | 0 | (41,632) |
| Temperature Sensitive Sales | 5,755,447 | 2,577,156 |
| Weather Factor - Warmer | 0.1174 | 0.1174 |
| Additional Sales | 675,881 | 302,644 |
| Average Revenue Per Rate Step | \$0.83428 | \$0.76742 |
| Additional Weather Normalization Revenue | <u>\$563,874</u> | <u>\$232,255</u> |

Increase in "Operating Revenue" for the Normalization of Weather for Midwest Gas Division

\$796,129

PEOPLES GAS DIVISION

| | Rate RS-1 | CS-2 |
|--|------------------|-----------------|
| Sales | 1,625,927 | 688,868 |
| Less Lost Load | 0 | (40,344) |
| Base Load | 276,180 | 165,004 |
| Less Lost Load | 0 | 0 |
| Temperature Sensitive Sales | 1,349,747 | 483,520 |
| Weather Factor - Warmer | 0.1174 | 0.1174 |
| Additional Sales | 158,505 | 56,781 |
| Average Revenue Per Rate Step | \$0.86893 | \$0.78953 |
| Additional Weather Normalization Revenue | <u>\$137,730</u> | <u>\$44,830</u> |

Increase in "Operating Revenue" for the Normalization of Weather for Peoples Gas Division

\$182,560

MIDWEST NATURAL GAS CORPORATION

**Detail of Adjustments
(WITNESS -MERCER)**

(1) REVENUE ADJUSTMENTS Continued

(c)

To decrease "Operating Revenue" for the loss of Large Commercial and Industrial load (\$2,166,584)

(d)

To decrease "Operating Revenue" for the reclassification of customers to the most correct rate class (\$28,603)

(e)

To adjust "Operating Revenue" for changes in the Base Cost of Gas Revenues.

| | RATE |
|---|-----------------------|
| Test Year Sales - Therms | 18,582,487 |
| Weather Normalization Additional Sales | 1,193,811 |
| Less: | |
| Reduction in customer usage | |
| Industrial | (1,105,838) |
| Interruptible | (1,317,289) |
| Large Commercial | (531,545) |
| Adjusted Test Year Sales - Therms | <u>16,821,626</u> |
| Pro-forma Cost of Gas | \$95,067 |
| Less: Unaccounted For Gas and Co Use | <u>95,067</u> |
| Base Rate Cost of Gas | <u>\$0</u> |
| New Base Rate Cost of Gas | <u>\$0.0000</u> |
| Prior Base Rate Cost of Gas Cause No. -Therm | <u>\$0.673988</u> |
| Net Change in Base Rate Cost of Gas | (0.673988) |
| Test Year Sales | <u>16,821,626</u> |
| Decrease in Operating Revenues Due to Reduction in Base Rate Cost of Gas | <u>(\$11,337,574)</u> |
| Total Adjustment (1) to "Operating Revenues" - Increase/(Decrease) | <u>(\$21,205,852)</u> |

MIDWEST NATURAL GAS CORPORATION

Detail of Adjustments
(WITNESS -MERCER)

(2) NATURAL GAS PURCHASED ADJUSTMENT

To adjust "Natural Gas Purchased" to eliminate the cost of natural gas to be purchased from base rates.

| | <u>RATE</u> | |
|---|--------------------|------------------------------|
| Test Year Sales - Therms | 18,582,487 | |
| Additional Purchases-Weather | 1,193,811 | |
| Less: Reduction of customer usage (adjustment 1(e)) | <u>(2,954,672)</u> | |
| Sub-Total | 16,821,626 | |
| Unaccounted for Gas Percentage - Test year | <u>0.53%</u> | |
| Estimated Unaccounted For Gas | <u>89,155</u> | |
| Estimated Purchases of System Gas | 89,155 | |
| Anticipated Cost of System Gas - Per Therm | <u>\$1.0663</u> | |
| Total Pro-forma Cost of Purchased Gas | \$95,067 | |
| Less: Test Year Purchased Gas | <u>21,398,968</u> | |
| Total Adjustment (2) to "Natural Gas Purchased" - Increase/(Decrease) | | <u><u>(\$21,303,901)</u></u> |

MIDWEST NATURAL GAS CORPORATION

Detail of Adjustments
(WITNESS -MANN)

(3) OPERATION & MAINTENANCE EXPENSE ADJUSTMENTS

(a)

To adjust other "Operation and Maintenance" Expense for the annualization of test year payroll and wage increases.

\$184,168

(b)

To adjust other "Operation and Maintenance" Expense for the amortization of rate case expense.

| | |
|-----------------------------------|-----------------|
| Original Estimate of Rate Case | \$200,000 |
| Mailing Expense | <u>\$7,000</u> |
| Estimated Cost of the rate case | \$207,000 |
| Amortization Period - Years | <u>3</u> |
| Annual Rate Case Expense | \$69,000 |
| Less: Test Year Rate Case Expense | <u>\$29,142</u> |

Adjustment - Increase/(Decrease)

\$39,858

(c)

To Adjust "Operation and Maintenance" Expense to reflect current IURC fee.

| | |
|--------------------------------------|--------------------|
| Applicable Revenues at Present Rates | \$23,004,076 |
| Current IURC Rate | <u>0.001062098</u> |
| Pro-forma Fee at Present Rates | \$24,433 |
| Less: Test Year IURC Fee | <u>26,704</u> |

Adjustment - Increase/(Decrease)

(\$2,271)

Total Adjustment (3) to "Operation and Maintenance" Expense - Inc./(Dec.)

\$221,755

MIDWEST NATURAL GAS CORPORATION

Detail of Adjustments
(WITNESS - MANN)

(4) ADMINISTRATIVE AND GENERAL EXPENSE ADJUSTMENTS

(a)

To adjust "Administrative and General" expense for the increase in the cost of property and casualty insurance.

| | |
|-----------------------------------|------------------------|
| Pro-forma Cost of Insurance | |
| Commercial Package | \$35,576 |
| Workers' Compensation | 22,927 |
| Commercial Umbrella | 29,248 |
| Auto Business | 27,875 |
| Pro-forma Cost of Insurance | <u>\$115,626</u> |
| Less: Test Year Insurance Expense | <u>104,528</u> |
| Adjustment - Increase/(Decrease) | <u><u>\$11,098</u></u> |

(b)

To adjust "Administrative and General" expense for the increase in the cost Employee Health, LTD and Life Insurance.

| | |
|--|------------------------|
| Pro-forma Monthly Employee Insurance Expense (Net of Employee) | \$10,297 |
| Number of Months | <u>12</u> |
| Pro-forma Employee Insurance Expense | \$123,567 |
| Less: Test Year Insurance Expense | <u>107,186</u> |
| Adjustment - Increase/(Decrease) | <u><u>\$16,381</u></u> |

(c)

To adjust "Administrative & General" expense for the increase associated with the contribution to the ESOP

\$11,050

(d)

To adjust "Administrative & General" expense for the elimination of the rent expense associated the purchase of the operational service building for the Scottsburg and Bloomfield offices.

(\$57,600)

(e)

To adjust "Administrative & General" expense for additional miscellaneous adjustments

| | |
|----------------------------------|------------------------|
| Communications Expense | \$13,236 |
| Public Awareness | 33,220 |
| Audit Expense | 17,500 |
| Office Expense | <u>271</u> |
| Adjustment - Increase/(Decrease) | <u><u>\$64,227</u></u> |

(f)

To adjust the "Administrative and General" expense for the requested amortization of the cost to implement the normal temperature adjustment procedures over 3 years

| | |
|------------------------------------|------------------------|
| Total Actual Cost | \$71,892 |
| Keystone - NTA Switch | <u>1,795</u> |
| | <u>73,687</u> |
| Amortization Period | <u>3</u> |
| Annual NTA Amortization Adjustment | <u><u>\$24,562</u></u> |

Total Adjustment (4) to "Administrative and General" Expense - Inc/(Dec) \$69,718

MIDWEST NATURAL GAS CORPORATIONDetail of Adjustments
(WITNESS - MANN)**(5) DEPRECIATION EXPENSE ADJUSTMENT**

To adjust "Depreciation Expense" to reflect current plant-in-service as of August 31, 2006.

| | | | |
|--|----------------|------------------|------------------------|
| Utility Plant-in-Service | | \$26,415,761 | |
| Less: | | | |
| Non-depreciable Property | \$506,488 | | |
| Transportation Equipment | 683,348 | | |
| Computer Equipment | 82,075 | | |
| Office Furniture | 100,203 | | |
| Tools | 34,835 | | |
| Power Operated Equipment | 182,558 | | |
| Communications Equipment | <u>121,490</u> | | |
| Total Deductions | | <u>1,710,997</u> | |
| Distribution Plant | | 24,704,764 | |
| Depreciation Rate | | <u>3.75%</u> | |
| Distribution Plant Depreciation | | | \$926,429 |
| Transportation and Computer Equipment | | 765,423 | |
| Depreciation Rate | | <u>20.00%</u> | |
| Transportation and Computer Equipment Depreciation Expense | | | 153,085 |
| Office Furniture, Tools, and Communications Equipment | | 439,086 | |
| Depreciation Rate | | <u>10.00%</u> | |
| Office Furniture, Tools, and Communications Equipment Depreciation Expense | | | <u>43,909</u> |
| Sub-Total Depreciation Expense | | | \$1,123,422 |
| Less: Test Year Depreciation Expense | | | <u>1,044,063</u> |
| Total Adjustment (5) to "Depreciation Expense" - Inc/(Dec) | | | <u><u>\$79,359</u></u> |

MIDWEST NATURAL GAS CORPORATION

**Detail of Adjustments
(WITNESS - MANN)**

(6) TAXES OTHER THAN INCOME TAXES

(a)

To adjust "Taxes Other Than Income Tax" for Increase
In FICA Tax for Payroll Increase reflected in adjustment 3(a).

\$12,861

(b)

To adjust "Taxes Other Than Income Taxes" to reflect changes
in Utility Receipts tax rates and applicable revenues.

Utility Receipt Tax

| | |
|----------------------------|----------------|
| Utility Receipts | \$5,157,582 |
| Less: Exemption | 1,000 |
| Bad Debts (2 year average) | <u>142,869</u> |

| | |
|--|--------------|
| Receipts Subject to Utility Receipts Tax | \$5,013,714 |
| Applicable Utility Receipts Tax Rate | <u>1.40%</u> |

| | |
|----------------------------|----------------|
| Pro-Forma at Present Rates | \$70,192 |
| Less: Test Year Expense | <u>366,199</u> |

Adjustment-Increase/(Decrease) in Utility Receipts Tax Expense (\$296,007)

Total Adjustment (6) to "Taxes Other Than Income Taxes" - Inc./(Dec.) (\$283,146)

MIDWEST NATURAL GAS CORPORATION

Detail of Adjustments
(WITNESS - MANN)

(7) INCOME TAX ADJUSTMENTS

To adjust "Income Tax" to reflect changes in
Revenues and Expenses

(a) STATE INCOME TAXES

| | | |
|---|------------------|--------------------------|
| Net Operating Income Before Taxes | (\$322,887) | |
| ADD: Utility Receipts Taxes | 70,192 | |
| LESS: Synchronized Interest | <u>(232,498)</u> | |
| State Taxable Income | | (\$485,193) |
| Applicable Rate | | <u>8.500%</u> |
| Pro-Forma at Present Rates | | (\$41,241) |
| Less: Test Year Expense - (Includes Gross Income Tax) | | <u>(29,829)</u> |
| Adjustment-Decrease in State Income Tax Expense | | <u><u>(\$11,412)</u></u> |

(b) FEDERAL INCOME TAXES

| | | |
|--|-----------------|------------------------|
| Net Operating Income Before Federal Tax and State Taxes | | (\$322,887) |
| Less: | | |
| Synchronized Interest | 232,498 | |
| State Income Tax | <u>(41,241)</u> | |
| Taxable Income | | (\$514,144) |
| Federal Tax Rate - Proposed | | <u>34.00%</u> |
| Pro-Forma Federal Income Tax Expense | | (\$174,809) |
| Less: Test Year Federal Income Tax | | <u>(213,151)</u> |
| Adjustment-Decrease in Federal Income Tax Expense | | <u><u>\$38,342</u></u> |
| Total Adjustment (7) to "Income Taxes" - Inc./Dec.) | | <u><u>\$26,930</u></u> |

MIDWEST NATURAL GAS CORPORATION

Detail of Adjustments
(WITNESS - MERCER)

Proposed Rate Increase Adjustments

(A)

To adjust "Operating Revenues" to reflect the requested revenue increase.

Pro-Forma Sale of Gas -

at Present Rates

\$23,004,076

Requested Increase

8.91%

Adjustment - Increase

\$2,048,995

(B)

To adjust "Other Operation and Maintenance" expense to reflect increase in IURC fee.

Increase in Revenue Requested

\$2,048,995

Current Effective Rate

0.106210%

Adjustment - Increase

\$2,176

(C)

To adjust "Administrative and General Expense" to reflect increase in bad debts

Increase in Revenue Requested

\$2,048,995

Current Effective Rate

0.004875199

Adjustment - Increase

9,989

TOTAL OTHER OPERATION AND MAINTENANCE

\$12,165

(D)

Increase in Revenue Requested

\$2,048,995

Less: Increase in Bad Debts

9,989

2,039,006

Applicable Utility Receipts Tax Rate

1.40%

Adjustment - Increase

\$28,546

MIDWEST NATURAL GAS CORPORATION

Detail of Adjustments
(WITNESS - MERCER)

Proposed Rate Increase Adjustments Continued

(E)

To adjust "State Income Tax" to reflect
changes in revenues and expenses.

| | |
|-------------------------------|--------------|
| Increase in Revenue Requested | \$2,048,995 |
| Less: Increase in bad debts | 9,989 |
| Less: Increase in IURC Fee. | <u>2,176</u> |
| Taxable Income | 2,036,830 |
| Applicable Tax Rate | <u>8.50%</u> |

Adjustment - Increase/(Decrease) in
"Supplemental Income Tax".

\$173,131

To adjust "Federal Income Tax" to reflect
changes in revenues and expenses.

| | |
|----------------------------------|----------------|
| Increase in Revenue Requested | \$2,048,995 |
| Less: Increase in IURC Fee. | 2,176 |
| Increase in Utility Receipts Tax | 28,546 |
| Increase in Bad Debt expense | 9,989 |
| Increase in State Income Tax | <u>173,131</u> |

| | |
|--|------------------|
| Federal Taxable Income - Increase | 1,835,153 |
| Plus: Federal Taxable Income - Present Rates | <u>(514,144)</u> |

| | |
|------------------------------|---------------|
| Total Federal Taxable Income | 1,321,009 |
| Federal Tax Rate - Proposed | <u>34.00%</u> |

| | |
|---|------------------|
| Pro-forma Proposed Rate Income Tax | 449,143 |
| Less: Pro-Forma Present Rate Income Tax | <u>(174,809)</u> |

Adjustment - Increase

623,952

Adjustment - Increase in Income Tax Expense

\$797,083

MIDWEST NATURAL GAS CORPORATION

TOTAL REVENUE CALCULATION

| | |
|-----------------------------------|--------------------|
| Estimated volume of gas purchased | 16,910,781 |
| Base Cost of Gas Estimated | <u>\$1.0663</u> |
| Base Cost of Gas Revenues | 18,032,212 |
| Pro-Forma Present Sales Revenues | <u>4,971,864</u> |
| Total Revenues | 23,004,076 |
| Requested Increase | <u>8.91%</u> |
| Revenue Adjustment - Overall | <u>\$2,048,995</u> |

MIDWEST NATURAL GAS CORPORATION

ORIGINAL COST RATE BASE

| | | |
|--|--------------|----------------------------|
| Utility Plant-In-Service as of August 31, 2006 | | \$26,415,761 |
| Less: Accumulated Depreciation | | <u>(15,489,505)</u> |
| Net Utility Plant-in-Service | | 10,926,256 |
| Plus: | | |
| Working Capital | 3,853,860 /8 | 481,733 |
| Materials and Supplies - 13 Month Average | | <u>454,138</u> |
| Total Original Cost Rate Base | | <u><u>\$11,862,127</u></u> |
| | NET INCOME | \$1,104,364 |

MIDWEST NATURAL GAS CORPORATION**CAPITAL STRUCTURE
AS OF AUGUST 31, 2006**

| Description | Amount | Percent of Total | Cost | Weighted Cost |
|--------------------|---------------------|---------------------------------|-------------|--------------------------|
| Common Equity | \$8,719,239 | 62.5145% | 11.75% | 7.35% |
| Long Term Debt | 3,874,242 | 27.7772% | 6.51% | 1.81% |
| Customer Deposits | 345,280 | 2.4756% | 6.00% | 0.15% |
| Deferred Taxes | <u>1,008,784</u> | <u>7.2327%</u> | 0.00% | <u>0.00%</u> |
| Total | <u>\$13,947,545</u> | <u>100.00%</u> | | <u>9.31%</u> |

MIDWEST NATURAL GAS CORPORATION**CALCULATION OF SYNCHRONIZED INTEREST
AS OF AUGUST 31, 2006**

| <u>Description</u> | <u>Amount</u> | <u>Percent of Total</u> | <u>Cost</u> | <u>Weighted Cost</u> | <u>Weighted Cost of Debt</u> |
|-----------------------|---------------------|---------------------------------|-------------|--------------------------|--------------------------------------|
| Common Equity | \$8,719,239 | 62.51% | 11.75% | 7.34% | |
| Long Term Debt | 3,874,242 | 27.78% | 6.51% | 1.81% | 1.81% |
| Customer Deposits | 345,280 | 2.48% | 6.00% | 0.15% | 0.15% |
| Deferred Taxes | <u>1,008,784</u> | <u>7.23%</u> | 0.00% | <u>0.00%</u> | |
| Total | <u>\$13,947,545</u> | <u>100.00%</u> | | <u>9.30%</u> | <u>1.96%</u> |
| Rate Base | \$11,862,127 | | | | |
| Weighted Cost of Debt | <u>1.96%</u> | | | | |
| Synchronized Interest | <u>\$232,498</u> | | | | |